

# **INITIAL STATEMENT OF REASONS**

## **Title 25, California Code of Regulations Chapter 7 Subchapter 2.5**

### **Proposed Adoption of a new Subchapter 2.5 Local Housing Trust Fund Program Sections**

**7150, 7151, 7152, 7153, 7154, 7155,  
7156, 7157, 7158, 7159, and 7160**

#### **I. Introduction & Background**

This Initial Statement of Reasons (ISOR) has been prepared by the California Department of Housing and Community Development (hereinafter “the Department”) to describe proposed regulations for the interpretation and implementation of the Local Housing Trust Fund program created by Health and Safety Code Section 50843.5<sup>1</sup> as modified by SB 586<sup>2</sup> and funded from the proceeds of the sale of bonds under the Housing and Emergency Shelter Trust Fund Act of 2006 (popularly known as “Proposition 1C”).<sup>3</sup>

The Department previously operated a local housing trust fund matching grant program pursuant to the provisions of Health and Safety Code Section 50843 utilizing funds provided by the Housing and Emergency Shelter Trust Fund Act of 2002 (“Proposition 46”). This program was operated utilizing guidelines rather than regulations as permitted by Health and Safety Code Section 50843(g).

In 2006, the Legislature passed AB 2638 which amended Health and Safety Code Section 50843 to provide that its provisions only applied to funds from Proposition 46. AB 2638 also enacted Section 50843.5 creating a slightly different local housing trust fund program (hereafter referred to as the “Section 50843.5 LHTF program”) subject to the availability of funding. Shortly thereafter, the voters passed Proposition 1C which allocated \$100 million to an Affordable Housing Innovation Fund subject to further legislative action.<sup>4</sup> In October 2007, the Legislature passed SB 586<sup>5</sup> which, among other things, stated:<sup>6</sup>

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<sup>1</sup> Sec. 4, Ch. 892, Stats. 2006, AB 2638.

<sup>2</sup> Sec. 3 of Ch. 652, Stats. of 2007, effective October 13, 2007, enacting Health and Safety Code Sec. 53545.9)

<sup>3</sup> Codified at Health and Safety Code Section 53540 et seq.

<sup>4</sup> See Health and Safety Code Section 53545(a)(1)(F).

<sup>5</sup> Ch. 652, Stats. of 2007, effective October 13, 2007.

<sup>6</sup> See Health and Safety Code Section 53545.9(c).

(c) The Department shall make available the amount of thirty-five million dollars (\$35,000,000) for the local housing trust fund matching grant program established under Section 50843.5. The Department shall make available 50 percent of this amount exclusively for newly established housing trust funds.

(1) When awarding grants from the funds allocated under this subdivision to existing trust funds, the department shall grant preference to a housing trust fund that agrees to expend more than 65 percent of state funds for the purpose of downpayment assistance to first-time homebuyers.

(2) When awarding grants from the funds allocated under this subdivision to newly established housing trust funds, the department shall set aside funding for a period of 36 months from the date funds are first made available for newly established housing trust funds that are in a county with a population of less than 425,000 persons.”

Hereafter, the generic term “local housing trust fund” will be abbreviated as “LHTF”. The Proposition 46-funded local housing trust fund matching grant program will be abbreviated as the “LHTFMG Program”. The specific local housing trust fund program described in the proposed regulations will be abbreviated as the “LHTF Program”.

## **II. General Approach to Regulations**

The Department generally was satisfied with the guidelines, application form, and state contract used to administer the LHTFMG Program. Therefore, the proposed regulations for the LHTF Program are based upon the previous guidelines, application form and state contract for the LHTFMG Program, modified to incorporate the additional provisions set forth in SB 586 and Health and Safety Code Section 50843.5.

In some cases, these regulations replicate or paraphrase statutory requirements. While this may appear duplicative of statute, these provisions are included in the proposed regulations to make the regulations user friendly by having all of the LHTF Program information in one place. Many of the Department’s customers do not have ready access to the printed California codes. In addition, the LHTF Program governing statutes are codified in two different widely-separated sections (Health and Safety Code Sections 50843.5 and 53545.9(c)) which could be confusing.

The organization of the subchapter generally follows the organization typically used by the Department for its loan and grant programs:

§7150.	Purpose and Scope.
§7151.	Definitions.
§7152.	Eligible Applicants.
§7153.	Eligible Use of Funds.
§7154.	Matching Fund Requirements.
§7155.	Application Requirements.
§7156.	Application Process.
§7157.	Protection of Program Funds.

§7158.	Encumbrance Deadline and Application of Repayments.
§7159.	Legal Documents.
§7160.	Reporting.

### III. Major Policy Decisions

#### A. Reliance on Previous Guidelines:

As noted above, the first major policy decision made by the Department was to base these proposed regulations on the LHTFMG Program guidelines. Generally the feedback the Department received on the prior program and guidelines was positive. In addition, prior to the release of these proposed regulations for formal public comment, the Department circulated a preliminary draft to stakeholders for their comments. These proposed regulations were developed with those stakeholder comments in mind.

#### B. Definition of “New Local Housing Trust Fund”:

The second major policy decision was the definition of “new local housing trust fund” which has been defined as a trust fund created and funded on or after September 30, 2006.

The original housing trust fund legislation<sup>7</sup> created the distinction between an existing LHTF and a “new” LHTF. AB 1891 enacting the LHTFMG Program became operative November 2002 and defined a “new” LHTF as a LHTF that came into existence on or after January 1, 2003.<sup>8</sup> According to the Assembly Floor Analysis of AB 1891, the purpose of this distinction was to encourage the creation of new LHTFs.<sup>9</sup>

SB 586 directs the Department to make Proposition 1C funds available “for the local housing trust fund matching grant program established under Section 50843.5.” Section 50843.5 permits the Department to define “new” LHTFs in the Notice of Funding Availability (“NOFA”).<sup>10</sup> Section 50843.5 became effective September 30, 2006. Rather than establishing the definition of “new” LHTF in each NOFA by fiat, the Department would rather invite public comment on the date, and then establish the date in regulation. LHTF Program NOFAs will then define “new” LHTF as stated in these regulations.

Following are the factors the Department considered in setting a date for establishment of “new” LHTFs:

- The purpose of distinguishing between new and existing LHTFs is to encourage the formation of new LHTFs. SB 586 has set aside half of the funds allocated to

<sup>7</sup> Health and Safety Code Sec. 50843.

<sup>8</sup> See Ibid. Subdiv. (b).

<sup>9</sup> See Assembly Floor Analysis of AB 1891, as amended August 13, 2002.

<sup>10</sup> See Health and Safety Code Sec. 50843.5(a)(2).

the LHTF Program for new LHTFs. Therefore, inducing the formation of new LHTFs is a high priority of the Legislature.

- The minimum grant to a LHTF is \$1 million, and the maximum grant is capped at \$2 million. In order to utilize 50% of the funds for new LHTFs, approximately 8 to 17 new LHTFs would have to be formed. In 2002 when the LHTFMG Program legislation passed, there were 10 city and 3 county LHTFs. In 2006, when AB 2638 was enacted, there were 21 city and 9 county LHTFs. (Perhaps this increase was due in part to the availability of Proposition 46 funds for new LHTFs.) Despite the increase in LHTFs between 2002 and 2006, the Department remains concerned that 8 to 17 new LHTFs may not be able to be formed within the time limits described below.
- Because of the match requirement, in order to receive a LHTF Program grant, a new LHTF must raise a minimum of \$1 million along with commitments for ongoing funding of the LHTF after the date established by the regulations for “new” LHTFs. The Department’s experience under the LHTFMG Program was that formation of LHTFs is a very difficult, time consuming process. Part of the difficulty is that it usually takes multiple sources, and perhaps even a group of local governments to create a viable LHTF.
- Proposition 1C requires that any LHTF Program funds not encumbered within 30 months of availability must revert to the CalHome program.<sup>11</sup> Funds are made available through the issuance of a NOFA. Therefore, parties interested in the formation of a “new” LHTF have 30 months to raise the \$1 million and submit an application. After approval of an application, funds will become encumbered upon the mutual execution of a state grant contract. Assuming that the LHTF Program regulations could become effective by July 1, 2008 and a NOFA was issued concurrently with the effective date, interested parties only would have approximately 24 months to encumber funds. Funds not committed for the LHTF Program by December 30, 2110 will revert to the CalHome program.
- The Legislature also has set a time limit of 36 months that funds will be made available for new LHTFs located in counties of less than 425,000 population.

Given the foregoing circumstances, the Department desires to make the window for formation of new LHTFs as wide as reasonably possible to ensure that the 50% funds set aside for new LHTFs can be encumbered within the prescribed time frame. For this reason, the Department has chosen September 30, 2006, the date that Section 50843.5 became effective.

During 2006, there was great publicity over several proposed infrastructure bonds, including a housing bond. The Proposition 1C bond bill (SB 1689) became effective May 17, 2006. It did not contain any express provisions for funding LHTFs. However,

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<sup>11</sup> See Health and Safety Code Sec. 53545(a)(1)(F).

\$100 million was set aside for future allocation by the Legislature to fund innovative housing programs. The Department is aware that during the discussions of SB 1689, and after the passage of Proposition 1C in November 2006, LHTF representatives were heavily involved in seeking funding for LHTFs. Therefore, it would not be unreasonable for LHTF advocates to begin considering formation of LHTFs in anticipation of future funding, which reasonably could have been anticipated to be allocated to the existing LHTFMG Program. The Department does not wish to hinder these efforts by setting a date in 2008 that would have the effect of requiring these fledgling LHTFs to compete for funds with older, well-established LHTFs.

#### **IV. Discussion of Specific Sections**

**Following is a discussion of each specific section of the proposed regulations. The proposed regulation will be shown in grayscale with the discussion following.**

##### **Adopt § 7150. Purpose and Scope.**

(a) These regulations implement and interpret Health and Safety Code Section 50843.5 and subdivision (c) of Health and Safety Code Section 53545.9.

(b) This program shall be known as the Local Housing Trust Fund Program.

It is customary and useful to the reader to begin a body of regulations with a statement of their authority, purpose and the general activities which they regulate. Existing regulations for 17 Department loan and grant programs were surveyed. Sixteen have initial sections titled “General,” “Purpose,” “Scope and Authority,” “Purpose and Scope,” etc. These sections provide information similar to that in Section 7150. Not to have a general introductory section would reduce the accessibility of the regulations and statutes to the user, and would have the benefit only of shortening the regulations by a fraction of a page.

##### **Adopt §7151. Definitions.**

The following definitions govern the use of the terms below in this subchapter:

(a) “Affordable Rent” means the same as defined in Health and Safety Code section 50053.

(b) “CCR” means the California Code of Regulations.

(c) “Department” means the Department of Housing and Community Development.

(d) “Dedicated Source” means taxes, fees, loan repayments, private contribution or other source of funds that will reasonably provide Ongoing Revenues to the Local Housing Trust Fund sufficient to meet the requirements of the Program.

(e) “Eligible Project” means any of the following:

(1) Rental housing projects or units within rental housing projects. The affordability of all units assisted by Program Funds shall be restricted for not less than 55 years.

- (2) Emergency shelters, safe havens, and transitional housing, as these terms are defined in Health and Safety Code section 50801.
- (3) Homeownership Project as defined in section 7151(j).
- (f) "Existing Local Housing Trust Fund" is a Local Housing Trust Fund organized, funded and operated prior to September 30, 2006.
- (g) "Extremely Low Income" has the meaning set forth in Health and Safety Code section 50106. Grantees shall utilize income limits issued by the Department for Extremely Low Income households for each county by household size.
- (h) "First-time Homebuyer" means an individual or individuals or an individual and his or her spouse who are in the process of buying a dwelling with the intent to occupy the home as a principal place of residence and who have not owned a home during the three-year period before the purchase of a home with Program Funds, except that the following individual or individuals may not be excluded from consideration as a first-time homebuyer under this definition:
- a. a displaced homemaker who, while a homemaker, owned a home with his or her spouse or resided in a home owned by the spouse. A displaced homemaker is an adult who has not, within the preceding two years, worked on a full-time basis as a member of the labor force for a consecutive twelve-month period and who has been unemployed or underemployed, experienced difficulty in obtaining or upgrading employment and worked primarily without remuneration to care for his or her home and family;
  - b. a single parent who, while married, owned a home with his or her spouse or resided in a home owned by a spouse. A single parent is an individual who is unmarried or legally separated from a spouse and has one or more minor children for whom the individual has custody or joint custody or is pregnant; or
  - c. an individual or individuals who owns or owned, as a principal residence during the three-year period before the purchase of a home with Program Funds, a dwelling unit whose structure is:
    - (A) not permanently affixed to a permanent foundation in accordance with local or state regulations; or
    - (B) not in compliance with state, local or model building codes and cannot be brought into compliance with such codes for less than the cost of constructing a permanent structure.
- (i) "Grantee" means an entity that has received an award of Program Funds.
- (j) "Homeownership Project" means a project in which Program Funds will be used to assist in the acquisition, construction or rehabilitation of owner-occupied housing units in which the homeowner has an ownership interest sufficient to secure the deed restriction required by subdivision (d)(3) of Health and Safety Code section 50843.5.
- (k) "Local Housing Trust Fund" is a public, joint public and private fund or charitable nonprofit organization described in Section 501(c)(3) of the Internal Revenue Code, which was established by legislation, ordinance, resolution (including nonprofit articles of incorporation) or a public-private partnership organized to receive specific revenue to address local housing needs. The key characteristic of a Local Housing Trust Fund is that it receives Ongoing Revenues from Dedicated Sources of funding sufficient to permit the fund to participate in the Program.
- (l) "Local Impact Fees" are impact fees, mitigation fees, or capital facility fees imposed on residential development by municipalities, county agencies, or other jurisdictions such as utility districts, school districts, water agencies and resource conservation districts. Local Impact Fees may include fees for residential or commercial development (in lieu of building affordable housing), parks and recreation, schools, traffic, street and signals, law enforcement facilities, fire facilities, library facilities, water facilities, waste water treatment, waste water collection,

drainage facilities, community development, general facilities, public facilities, governmental, environmental, and facilities assessments.

- (m) "Lower Income Households" has the meaning set forth in Health and Safety Code section 50079.5. Grantees shall utilize limits issued by the Department for Lower Income Households. For each county by household size
- (n) "Matching Funds" shall mean available funds meeting the requirements of section 7154.
- (o) "Moderate Income Persons and Families" has the meaning set forth in Health and Safety Code section 50093, subdivision (b).
- (p) "New Local Housing Trust Fund" is a Local Housing Trust Fund that was created, funded and operated on or after September 30, 2006.
- (q) "NOFA" means a Notice of Funding Availability issued by the Department to announce the availability of Program Funds, the terms and conditions of awards and requirements for the submittal of applications.
- (r) "On Deposit" means cash or equivalent under the control of the applicant or Grantee at the time of application readily available for use by the Grantee as Matching Funds. Funds On Deposit must be verifiable at the time of application to the satisfaction of the Department.
- (s) "Ongoing Revenues" means a public source of revenue that is dedicated for an indefinite period (beyond annual appropriations); or other revenue that is dedicated for a minimum five year period and the source of that revenue has an income history which can reasonably support the level of proposed funding.
- (t) "Program" or "LHTF Program" means the Local Housing Trust Fund Program authorized by Health and Safety Code section 50843.5 as implemented in this subchapter.
- (u) "Program Funds" means the funds provided by the Department to a Local Housing Trust Fund pursuant to this subchapter. Each award of Program Funds to a Local Housing Trust Fund shall equal at least one million dollars and shall not exceed two million dollars.
- (v) "Very Low Income" has the meaning set forth in Health and Safety Code section 50105. Grantees shall utilize income limits issued by the Department for Very Low Income households for each county by household size.

It is customary and useful to the reader to begin a body of regulations with definitions of key terms used throughout the body of regulations. The definitions in this section as closely as possible mirror the way the terms are used in statute. Specific references to statute and regulation have been included within the respective definitions as applicable. Definitions not based on statute or regulations are definitions customarily used within the low-income housing industry.

The Department received comments from stakeholders concerning the definition of "On Deposit." A concern was expressed that if the Department took literally the requirement that matching funds be "on deposit" at time of application, as implied by subparagraph (c) of Health and Safety Code section 50843.5, a LHTF might be precluded from using a verifiable line of credit as the match. In such a situation, the LHTF could draw down on the line of credit to have the match "on deposit," however; doing so would result in the LHTF needlessly incurring addition interest, as the funds sitting on deposit in the LHTF's

bank account may not be awarded to a qualified project for several months after the LHTF submits its application for a Program grant. The Department decided to define “on deposit” to include verifiable, readily available funds to accommodate line of credit and other verifiable, readily available sources of funding commonly used in the low-income housing industry.

**Adopt §7152. Eligible Applicants.**

The following entities shall be eligible to apply for Program funds:

(a) A city, county, or city and county that has created, funded, and operated an Existing Local Housing Trust Fund, or that has created and funded a New Local Housing Trust Fund.

(1) The trust fund shall have the following characteristics:

(A) It shall consist of a public or joint public and private fund established by legislation, ordinance, resolution, or a public-private partnership to receive specific revenue to address local housing needs.

(B) It shall be funded from Ongoing Revenues from Dedicated Sources of funding such as taxes, fees, loan repayments, or private contributions.

(2) The city, county, or city and county shall have, at the time of application an adopted housing element that the Department has determined, pursuant to Section 65585 of the Government Code, is in substantial compliance with the requirements of Article 10.6 (commencing with Section 65580) of Chapter 3 of Division 1 of Title 7 of the Government Code.

(3) A Local Housing Trust Fund that was created, funded, and operated by a combination of one or more cities or counties, shall in its application, agree to utilize Program Funds only for Eligible Projects located in cities or counties that have, at the time of application, an adopted housing element meeting the requirements of subparagraph (2) above,

(b) A charitable nonprofit organization described in Section 501(c)(3) of the Internal Revenue Code that has created, funded, and operated an Existing Local Housing Trust Fund, or has created and funded a New Local Housing Trust Fund.

(1) The trust fund shall have the following characteristics:

(A) It shall consist of a public or joint public and private fund established by legislation, ordinance, resolution, or a public-private partnership to receive specific revenue to address local housing needs.

(B) It shall be funded from Ongoing Revenues from Dedicated Sources of funding such as taxes, fees, loan repayments, or private contributions.

(2) The charitable nonprofit organization shall, in its application, agree to utilize Program Funds only for Eligible Projects located in cities, counties, or a city and county that have, at the time of application, an adopted housing element that the Department has determined, pursuant to Section 65585 of the Government Code, to be in substantial compliance with the requirements of Article 10.6 (commencing with Section 65580) of Chapter 3 of Division 1 of Title 7 of the Government Code.



The provisions of this section are taken directly from Health and Safety Code Section 50843.5, organized in a clearer, more user-friendly manner.

**Adopt §7153. Eligible Use of Funds.**

(a) Funds shall be used by the Grantee to provide loans for payment of predevelopment expenses, acquisition, construction, or rehabilitation of Eligible Projects.

(b) At least 30 percent of the total amount of the Program Funds and the Matching Funds shall be expended on Eligible Projects that are affordable to, and restricted for, Extremely Low Income households. No more than 20 percent of the total amount of the Program Funds and the Matching Funds shall be expended on Eligible Projects affordable to, and restricted for, Moderate Income Persons and Families. The remaining Program Funds and Matching Funds shall be used for Eligible Projects that are affordable to and restricted for, Lower Income Households.

(c) No Program Funds shall be used for the costs of administering the Local Housing Trust Fund.

The eligible uses of LHTF Program funds are set forth in subdivisions (d)(1) and (2) of Health and Safety Code section 50843.5 and are repeated in regulation for convenience and clarity. Local administrative costs are not listed as an eligible expense under the statute and subsection (c) of the proposed regulation makes it clear that administrative costs of the LHTF are not a permissible use of LHTF Program funds.

**Adopt §7154. Matching Fund Requirements.**

(a) For each Program grant applicants shall provide Matching Funds equal to or in excess of the amount of the Program grant.

(b) Matching Funds shall be On Deposit at the time of application, and the source of the funds shall be identified.

(c) Funds restricted for housing use by state or federal law (such as funds from the Home Investment Partnerships Program (HOME), the Community Development Block Grant Program (CDBG), or redevelopment agency low- and moderate-income housing fund set-aside ("LMIHF") funds) shall not be considered Matching Funds. However, redevelopment agency non-LMIHF funds may be considered Matching Funds.

(d) A Local Housing Trust Fund that is exclusively funded by any combination of HOME, CDBG, redevelopment agency LMIHF funds, or other funds restricted for housing use shall not be eligible to receive Program Funds.

Subdivision (c) of Health and Safety Code section 50843.5 requires that all LHTF Program funds be matched on a dollar-for-dollar basis with funds currently available and identifiable. Furthermore, the statute requires that matching funds cannot be funds that are required by any state or federal law to be spent on housing. The proposed regulation gives examples of funds that do not meet the match requirement because they are restricted for housing use and further makes it clear that a LHTF funded exclusively by funds restricted for housing use is not an eligible applicant.

**Adopt §7155. Application Requirements.**

Application for Program funds shall be made in a format provided by the Department. The Department shall request the following information:

(a) Applicant identification information including: name, address, telephone number, contact person and, for nonprofit corporations, corporate governing documents and financial information (e.g., articles of incorporation and by laws, certificate of good standing, confirmation of 501(c)(3) status, audited financial statements), identification of the administering entity, and list of legislative representatives for the area where the program or project will be undertaken.

(b) Governing board resolution in a form acceptable to the Department authorizing the application.

(c) Description of the Local Housing Trust Fund sufficient to ensure compliance with Health and Safety Code Section 50843.5 and this subchapter which at a minimum shall include:

- (1) Documentation of establishment.
- (2) Date of establishment.
- (3) Date first funding received.
- (4) Ongoing Revenue sources (distinguishing residential and non-residential Local Impact Fees).
- (5) Documentation of Matching Funds On Deposit.
- (6) Documentation of sufficient Ongoing Revenues.
- (7) Documentation of the amount and source of Matching Funds and evidence that Matching Funds are derived from sources that are not restricted to housing uses.

(d) Local Housing Trust Fund operating guidelines including:

- (1) Types of projects in which the fund will invest.
- (2) Types of investments the fund will make (e.g., loans, grants).
- (3) The required terms and conditions of the investment, including types of security and regulatory agreements, and periods of affordability.
- (4) Any per unit or per project expenditure limitations.
- (5) The eligible household income limitations and/or income targeting goals.
- (6) The developer or owner eligibility requirements.
- (7) Underwriting requirements.
- (8) The borrower or project match or leverage requirements.
- (9) Geographic area to be served.

(e) Amount of Program Funds applied for and the amount to be used for: First-time Homebuyer downpayment assistance; housing for persons or households of Extremely Low Income, Very Low Income; Lower Income Households and housing for Moderate Income Persons and Families.

(f) Description of the management and staffing of the Local Housing Trust Fund.

(g) If the applicant proposes to use Program Funds for rental housing projects, a copy of the document to be recorded restricting the affordability of Program-funded projects for at least 55 years.

(h) If the applicant proposes to use Program Funds for Homeownership Projects, a copy of the document to be recorded that meets the requirements of subdivision (d)(3) of Health and Safety Code Section 50843.5 or a specific statement as to the other public funding source or law in conflict with this requirement.

(i) Certifications and Acknowledgements:

- (1) Certification that the information submitted in the application is true and correct to the best of the knowledge of the signer, after reasonably diligent investigation.
- (2) Certification of the applicant's intent to maintain the Local Housing Trust Fund in existence for at least five (5) years from the date of application; and acknowledgement and agreement that if the Local Housing Trust Fund ceases to exist sooner, then the applicant agrees to repay any remaining uncommitted Program Funds and to remit to the Department all repayment of loans made with Program Funds until the full amount of the Program grant is repaid.
- (3) Acknowledgement and agreement that any Program Funds that are not encumbered within 36 months of receipt shall be returned to the Department.
- (4) For nonprofit applicants, an acknowledgement and agreement that Program Funds shall be used only for projects located in a city, county, or city and county that have, at the time of application, an adopted housing element that the Department has determined to be in substantial compliance with State housing element law.
- (5) Certification that the applicant has held, or agrees to hold, at least one public hearing to discuss and describe the Eligible Project or Projects that will be financed with Program Funds.
- (6) For nonprofit applicants, an agreement that the applicant will hold at least one public meeting as required by subdivision (g) of Health and Safety Code section 50843.5.

For ease in processing applications for grants under the program, it is beneficial to the applicants and the Department to set out basic application information requirements in the regulations. The items required in the proposed regulation are typical of most other programs administered by the Department.

#### **Adopt §7156. Application Process.**

(a) For New Local Housing Trust Funds, the Department periodically shall issue a NOFA that specifies, among other things, the total amount of funds available, the total amount of funds available for New Local Housing Trust Funds in counties of less than 425,000 persons, the terms and conditions of the award of Program Funds and the final deadline for application. Applications will be accepted on an over-the-counter basis, and "complete" applications, as described in subsection (b)(1), will be funded on a first come-first serve basis until funds are exhausted, or the final deadline has expired, whichever occurs sooner. In the event that insufficient funds are available to fund all complete applications received on the same date, the applications will be evaluated and funded based on the criteria set forth in subdivision (b)(2), except there will be no preference given for meeting the requirement of subdivision (b)(2)(A).

(b) For Existing Local Housing Trust Funds, the Department shall periodically issue a NOFA that specifies, among other things, the amount of funds available, the terms and conditions of the award of Program Funds, and the application deadline.

(1) Only complete applications shall be considered for funding. In order to be considered "complete" an application must have substantially all of the information requested and provide adequate documentation and information for the Department to determine the Local Housing Trust Fund's eligibility for funding pursuant to Health and Safety Code Section 50843.5 and this subsection. The applicant shall bear the burden of demonstrating compliance with these requirements.

(2) In the event that the amount of funding requested in complete applications exceeds the funds available, applications shall be evaluated and funded using criteria published in the NOFA, including, but not limited to the following, with a preference given to applications to the extent they meet the requirements of (A) and (B);

- (A) The extent to which the applicant agrees to expend more than 65 percent of its Program Funds for the purpose of providing downpayment assistance to First-time Homebuyers.
- (B) The extent to which the applicant agrees to provide Matching Funds from sources other than residential Local Impact Fees.
- (C) The extent to which the applicant agrees to expend more than 30 percent of its Program Funds and Matching Funds to serve persons and families of Extremely Low Income and Very Low Income .
- (D) The extent to which the applicant agrees to expend less than 20 percent of its Program Funds and Matching Funds to serve persons and families with incomes exceeding 120 percent of the area median income.
- (E) The extent to which the applicant agrees to provide Matching Funds in excess of the amount of Program Funds.

It is customary to set out the general application process in regulation. In addition to the general process used in other Department programs, this section attempts to consolidate into the application process and clarify statutory set-aside and priority requirements. To accommodate the set-aside and preference requirements of subsection (c) of Health and Safety Code section 53545.9, the Department will be setting up separate NOFAs as to new and existing LHTFs. Subsection (c) of Health and Safety Code section 53545.9 requires that 50% of program funds be awarded to new LHTFs and subsection (c)(1) sets up a preference for existing LHTFs that agree to expend more than 65% of state funds for first-time homebuyer assistance. Subsection (c)(2) of Health and Safety Code section 53545.9 requires a 36 month set-aside for new LHTFs in counties with a population of less than 425,000. Subsection (a)(1) of Health and Safety Code section 50843.5 provides an application priority for LHTFs with a matching fund source other than impact fees on residential development. The proposed regulation organizes the application requirements into subparagraph (a) for new LHTFs and subparagraph (b) for existing LHTFs. This organization is an attempt to apply the statutory set-asides and preferences and should facilitate applicants' understanding of the applicable requirements.

#### **Adopt §7157. Protection of Program Funds.**

- (a) In order protect the Program Funds awarded to a Grantee, the Grantee shall provide the Program Funds in the form of a loan evidenced by a promissory note the repayment of which shall be secured by a deed of trust recorded on the property being assisted with Program Funds. The promissory note shall contain a special provision that repayment shall be made to the Department in the event that the Grantee is no longer in operation.
- (b) Where Program Funds are provided to a rental housing development, emergency shelter, safe haven or transitional housing:
  - (1) The Grantee and the housing developer borrower shall enter into a development loan agreement setting forth the terms and conditions for closing and disbursing the Program Funds which shall include, but not be limited to, requirements for title insurance for the deed of trust, and the borrower's responsibilities and obligations with respect to hazardous substance detection, disclosure, and remediation.
  - (2) The Grantee shall submit copies of all loan guidelines and underwriting standards and procedures for review by the Department.

- (3) The Department shall have the right to request copies of documentation of the activities of the Local Housing Trust Fund at any time prior to or after disbursement of Program Funds.

(c) Where Program Funds are used to acquire, construct or rehabilitation for sale housing the Grantee shall record a deed restriction in compliance with Health and Safety Code section 50843.5(d)(3).

These provisions were included in the Department's LHTFMG Program agreement with grantees. The funds provided for the LHTF Program by SB 586 come from the sale of general obligation bond funds. It is the responsibility of the Department to ensure that these funds are used responsibly. While Health and Safety Code Section 50843.5 does not expressly state that LHTFs shall use Program funds to make loans, there is clear evidence that this is what the Legislature intended. One of the characteristics of a LHTF is that the fund is continually replenished through on-going dedicated revenue sources and loan repayments (see Sec. 50843.5(b)(2)). Also, loan repayments are to accrue to the grantee LHTF unless the trust no longer exists, in which case, the repayments are to accrue to the Department (subdiv. (e) of Sec. 50843.5)).

Subdivision (a) of the proposed regulation is included to make clear to grantees that LHTF Program funds are to be made available in the form of secured loans. Requiring the loan be secured by the real property assisted protects the state's funds.

Subdivision (b) is necessary to set forth typical Department lending practices for rental housing developments to protect state funds.

Subdivision (c) covers for-sale housing, which requires a deed restriction (Health and Safety Code section 50843.5(d)(3)).

#### **Adopt §7158. Encumbrance Deadline and Application of Repayments.**

(a) Any Program Funds not encumbered by a Grantee by a loan commitment to the developer of an Eligible Project within 36 months of receipt shall promptly be returned to the Department.

(b) Repayments of Program Funds received by a Grantee shall be retained by the Grantee in the Local Housing Trust Fund to be used for the purposes set forth in this subchapter.

(c) If a Grantee ceases operations or Ongoing Revenues cease less than five years from the date of the Grantee's award of Program Funds, all unencumbered Program Funds shall promptly be returned to the Department, and all current and future loan repayments shall be remitted to the Department.

(d) The total amount paid to the Department pursuant to (a) and (c) above and Section 7157(a) shall not exceed the amount of the Program Funds received by the Grantee.

The provisions of this section are drawn from the statutory provisions of subdivisions (c), (e) and (i) of Health and Safety Code section 50843.5. They are included in the regulations to ensure that they are not overlooked by grant recipients; to put each recipient on notice of the requirements; and to make the regulations more user friendly by having most of the regulatory and statutory provisions in one place.

Subsection (d) was added in response to comments received from stakeholders for clarification that all repayments to the state based on the grant of program funds will never exceed the total of the LHTF Program grant. Stakeholders were concerned that requiring repayment of more than the grant amount would violate agreements with other funding sources. Subparagraph (d) makes this clear and is consistent with the various requirements of Health and Safety Code section 50843.5.

**Adopt §7159. Legal Documents.**

Upon the award of funds the Department shall enter into a standard agreement with the Grantee constituting a conditional commitment of funds. The standard agreement shall require the Grantee to comply with the requirements and provisions of these regulations and Health and Safety Code section 50843.5 and shall, in addition, contain the following:

- (a) Encumbrance deadlines; project completion deadlines; and agreement termination date.
- (b) Grantee contract coordinator.
- (c) Disbursement conditions and documentation.
- (d) Remedies.
- (e) Insurance and inspection requirements.
- (f) Record retention and reporting requirements.
- (g) Prevailing wage requirements as applicable.

Prior to the disbursement of state funds, it is a practical necessity to pin down all significant terms and conditions in an agreement that if necessary can be enforced in court. The agreement also serves as the formal document for encumbering state funds. The specific information to be included has been taken from the agreement the Department used for the LHTFMG Program.

(a) -- Local encumbrance deadlines are necessary to comply with the requirement of subdivision (i) of Health and Safety Code Section 50843.5 which requires that a LHTF encumber Program funds no later than 36 months after receipt. All contracts need to have a termination date. It is necessary to memorialize completion deadlines to help ensure that project funds will be utilized and affordable housing produced within a reasonable time frame.

(b) -- For administrative efficiency, the grantee needs to designate a contact person in the event the Department has questions concerning the grant.

(c) -- Both the Department and the grantee need to have a clear understanding of the method that Program funds will be disbursed.

(d) --In order to ensure that the state can take steps to recover grant funds in the event of a violation of the Program statute or regulations, the agreements must include remedies.

(e) -- To ensure the state's investment in affordable housing projects assisted with Program funds, the Department routinely imposes insurance and inspection requirements in its loan and grant agreements.

(f) – All of the Department's loan and grant agreements contain requirements for record retention and reporting in order to assure the state's ability to audit grantees to ensure that state funds have been properly expended and accounted for.

(g) – If LHTF Program funds are expended on a “public work” prevailing wages must be paid. Occasionally the Department finds that a loan or grant recipient is unfamiliar with the requirements of state prevailing wage laws. The purpose of including this provision in the LHTF Program agreement is to ensure that grantees do not overlook this requirement.

#### **Adopt §7160. Reporting.**

Not later than October 1 of each year a Grantee shall provide to the Department an annual report, in a format specified by the Department, containing the following information:

(a) A narrative summary of the Local Housing Trust Fund activities including:

- (1) Work undertaken or completed in the reporting period, including the number, type and size of Eligible Projects receiving the proceeds of Program Funds.
- (2) Activities planned to be undertaken in the next reporting period.
- (3) Description of problems encountered in Program implementation; and a description of solution and timing of solution.
- (4) Description of how problems may impact ability to complete or fulfill obligations under the standard agreement.
- (5) Description of any technical assistance desired from the Department.

(b) Financial summary including:

- (1) Amount of Program Funds available at the beginning of the reporting period, the amount drawn down to date, and the remaining balance.
- (2) Documentation of Matching Funds, including the amount by source, expended during the reporting period.

(c) A summary of Eligible Projects assisted during the reporting period, including the project name, number of units, income levels assisted, and amount of Program Funds expended per unit.

Health and Safety Code section 53545(a)(4) requires the Department to annually report how Proposition 1C funds are allocated and expended. The LHTF Program is funded from funds made available under the Affordable Housing Innovation Fund portion of Proposition 1C (see Sec. 53545(a)(1)(F)). Since funds are to be used for programs that demonstrate innovative, cost-saving approaches to creating or preserving affordable housing, it is necessary to gather information about the LHTF Program's achievements in order to determine the viability of LHTFs as a means of providing affordable housing. Finally, subdivision (j) of Health and Safety Code section 50843.5 requires recipients of LHTF Program funds to file periodic reports with the Department regarding the use of Program funds. The Department is required to report to the Legislature no later than December 31 of each year regarding: the number of trust funds created; a description

of the projects supported; the number of units assisted; and the amount of matching funds received.

The provisions of proposed regulation section 7160 are designed to gather the foregoing required information. An annual reporting date of October 1<sup>st</sup> has been selected in order to give the Department time to pull all of the Program participants' reports together and then summarize the information for the report to the Legislature. The specific pieces of information requested are the same as requested by the Department under the LHTFMG Program and did not pose a problem or excessive burden on participants.